has had to infer what Congress might have done had it considered the question. *Id.* This was because "Congress did not create a private § 10(b) cause of action and had no occasion to provide guidance about the elements of a private liability scheme." *Id.*

*Central Bank* lists *Blue Chip Stamps* as a decision within the second category, a decision in which Section 10(b)'s statutory text did not control the decision because Congress had provided no "guidance." *Id.* at 172. Because the purchaser-seller requirement recognized in *Blue Chip Stamps* is not imposed by Section 10(b)'s "in connection with" language, and this Court had long made clear that it is not, Congress' borrowing of that language for SLUSA cannot be understood as evidencing an intention to import the purchaser-seller limitation into its definition of SLUSA's preemptive reach. Indeed, it would be ironic if *Blue Chips Stamps'* limitation, which precludes the private securities actions this Court thought most likely to be vexatious, were the mechanism for limiting Congress' efforts to preclude state securities class actions it found vexatious and abusive.

## II. SLUSA'S "IN CONNECTION WITH" LANGUAGE REQUIRES ONLY THAT THE MISCONDUCT INVOLVE SECURITIES TRANSACTIONS.

Section 10(b)'s and Rule 10b-5's "in connection with" language has consistently been read to reach conduct connected to *anyone's* securities transactions, rather than limited to conduct connected to *plaintiffs'* purchases or sales. SLUSA's use of that language, without providing for a different meaning, precludes a narrower construction of SLUSA's "in connection with" language. That textual reading is also supported by the statute's purpose and legislative history.

### A. The Borrowed Language Defines Claims In Which the Alleged Misconduct Coincides With Securities Transactions.

The established judicial construction of Section 10(b)'s and Rule 10b-5's "in connection with" requirement is that it requires only that the alleged fraud coincide with securities transactions. It does not require that the plaintiffs themselves purchased or sold the securities at issue or, therefore, that plaintiffs in a class action purchased the securities during the class period. Section "10(b) bans the use of any deceptive device in the 'sale' of any security by *'any person.'* " *Superintendent of Insurance v. Bankers Life & Casualty Co.*, 404 U.S. 6, 10 (1971) (emphasis added).

Thus, *United States v. O'Hagan*, 521 U.S. 642, 656 (1997), ruled that Section 10(b)'s "in connection with" requirement was satisfied by the *defendant's* purchase of securities. The requirement was satisfied because attorney O'Hagan's breach of duty to his firm's client coincided with his *own* purchases of securities. *Id.* The Court explained that the "provision, as written, does not confine its coverage to deception of a purchaser or seller of securities." *Id.* at 651. Section 10(b) may be violated "even though the person or entity defrauded is not the other party to the trade." *Id.* at 656.

Similarly, in *SEC v. Zandford*, 535 U.S. 813, 822 (2002), the Court ruled that a broker's sale of his client's securities and theft of the proceeds, without the client's knowledge, met the "in connection with" requirement because: "It is enough that the scheme to defraud and the sale of securities coincide." *See also Carpenter v. United States*, 484 U.S. 19, 24 (1987) (affirming, by divided vote, the conviction under Section 10(b) and Rule 10b-5 of a newspaper columnist, based on securities trades by his *co-participants*, because the columnist had breached his duty to his newspaper by passing on confidential information, even though "the victim of the fraud, the Journal, was not a buyer or seller of the stocks traded in or otherwise a market participant").

Moreover, in these cases, as in other enforcement proceedings under Section 10(b) and Rule 10b-5, none of the securities transactions found to meet the "in connection with" requirement were purchases or sales by the *plaintiff*. In such proceedings, the plaintiff is a government agency. Although, in each case, this Court required that the misconduct alleged must be "in connection with" securities transactions, it has never required that the plaintiff be the purchaser or seller. *See, e.g., United States v. Naftalin,* 441 U.S. 768 (1979).

### B. The Statutory Text Precludes Adding A Purchaser-Seller Restriction.

When Congress borrowed Section 10(b)'s "in connection with" language for SLUSA, it intended the phrase to mean for SLUSA purposes what it means for Section 10(b) and Rule 10b-5 purposes. *See, e.g., Bragdon v. Abbott,* 524 U.S. 624, 632 (1998) ("Congress' repetition of a well-established term carries the implication that Congress intended the term to be construed in accordance with pre-existing . . . interpretations."); *Lorillard v. Pons,* 434 U.S. 575, 581 (1978) (Congress "can be presumed to have had knowledge of the interpretation given to the incorporated law."). Congress is understood to have "adopted" the pre-existing interpretations unless it provides otherwise. *See Keene Corp. v. United States,* 508 U.S. 200, 212 (1993).[3]

Thus, the meaning of Section 10(b)'s "in connection with" language provides its meaning for SLUSA. All six of the Courts of Appeals to address the question have reached

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[3] Here, the presumption is particularly appropriate because the "old" and "new" laws are sections of both the same and related statutes. *See, e.g., Gustafson v. Alloyd Co.,* 513 U.S. 561, 570 (1995) (adhering to "the normal rule of statutory construction that identical words used in different parts of the same act are intended to have the same meaning") (quotations omitted); *Brooke Group Ltd. v. Brown & Williamson Tobacco Corp.,* 509 U.S. 209, 229-30 (1993) (relying on long-settled meaning of Clayton Act language to interpret identical phrase in Robinson-Patman Act).

the same conclusion. *See Kircher*, 403 F.3d at 482 (noting that "[e]very court of appeals to encounter SLUSA has held that its language has the same scope as its antecedent in Rule 10b-5") (citing decisions from the Second, Third, Eighth, Ninth and Eleventh Circuits and adding the Seventh Circuit to that consensus).

As discussed above, the meaning of Section 10(b)'s "in connection with" requirement—and, thus, SLUSA's—is that the misconduct alleged must be in connection with *someone's* securities transactions. It need not be in connection with plaintiffs' transactions, much less plaintiffs' transactions during the class period. *See, supra*, Pt. II.A.

Nothing in SLUSA's text offers a toehold for narrowing SLUSA's preemptive reach. Congress was certainly aware of the long-recognized judicially-imposed purchaser-seller requirement on private suits under Section 10(b) and Rule 10b-5, and "knew how to impose [a purchaser-seller requirement] when it chose to do so." *Central Bank*, 511 U.S. at 176. Only ten years before enacting SLUSA, Congress provided a private right of action to recover losses caused by insider trading and expressly limited such suits to contemporaneous purchasers and sellers. *See* Insider Trading and Securities Enforcement Act of 1988, P.L. 100-704, 102 Stat. 4677, 4680-81, *codified at* 15 U.S.C. § 78t-1(a) (confining application to "any person who, contemporaneously with the purchase or sale of securities that is the subject of such violation, has purchased . . . or sold . . . securities of the same class").

Congress did not adopt this language, or *any* language, to similarly limit SLUSA's reach. Had Congress intended to limit SLUSA's application to suits alleging misconduct in connection with plaintiffs' securities transactions, it could have done so by changing only one word. It could have drafted the requirement to provide: "in connection with *plaintiff's* purchase or sale of a covered security" instead of *"the"* purchase or sale. It did not do so.

Congress could also have incorporated such a limitation in SLUSA by defining "covered class actions" to include only lawsuits brought by the purchasers or sellers of the securities. Again, Congress did not do so. Congress could have included—in the long list of carefully delineated exceptions that Congress *did* provide – an express exception for suits under state law brought by non-purchaser-sellers. *See* 15 U.S.C. §§ 78bb(f)(3), (f)(4), (f)(5)(C). But Congress did not do that either.

Congress' use of language with a well-settled meaning, without including any provision narrowing that meaning, precludes addition of a narrowing construct. Courts "begin with the understanding that Congress says in a statute what it means and means in a statute what it says there." *Hartford Underwriters Ins. Co. v. Union Planters Bank, N.A.*, 530 U.S. 1, 6 (2000) (quotation omitted). When, as here, "the statute's language is plain, the sole function of the courts—at least where the disposition required by the text is not absurd—is to enforce it according to its terms." *Id.* (quotations omitted).

### C. Applying the Settled Meaning of "In Connection With" to SLUSA Preemption Would Not Lead to Absurd Results.

Literal application of the "in connection with" provision is not even *outside* Congress' purposes, much less "demonstrably at odds" with them. *See Griffin v. Oceanic Contractors, Inc.*, 458 U.S. 564, 571 (1982) (noting that courts may override statutory language only in the rare case where "the literal application of a statute will produce a result demonstrably at odds with the intentions of its drafters").

Rather, it would affirmatively further the purposes for which Congress enacted SLUSA, by helping to ensure that securities lawsuits are able to impose costs on the securities markets only if they are sufficiently meritorious to survive the gatekeeping mechanisms Congress has chosen to rely

on. SLUSA was intended to make "Federal court the exclusive venue for most securities class action lawsuits." H. R. Conf. Rep. No. 105-803, at 13 (1998) ("Conf. Rep."). "The legislation is designed to protect the interests of shareholders and employees of public companies that are the target of meritless 'strike' suits. The purpose of these strike suits is to extract a sizeable settlement from companies that are forced to settle, regardless of the lack of merits of the suits, simply to avoid the potentially bankrupting expense of litigating." *Id.* Applying the terms of the statute furthers these purposes by requiring private class action plaintiffs who complain of being deceived to bring federal securities fraud suits subject to federal procedural safeguards, and private class action plaintiffs who complain of corporate mismanagement to bring derivative suits, which are expressly exempted from SLUSA preemption but subject to state law procedural safeguards.

Although the primary impetus for SLUSA was an interest in staunching the increasing flow of securities class actions brought in state courts to avoid the strictures Congress had imposed three years earlier in the PSLRA,[4] the statute Congress enacted is broader. *See* SLUSA, 112 Stat. at 3227, 3228, 3230. Indeed, it is commonplace for Congress to have focused on the need to respond to a particular problem but to enact broader legislation. *See Brogan v. United States,* 522 U.S. 398, 403 (1998) (recognizing "the reality that the reach of a statute often exceeds the precise evil to be eliminated"). When Congress enacts broader legislation, as this Court has repeatedly explained, "it is not, and cannot be, our practice to restrict the unqualified language of a statute to the particular evil that Congress was trying to remedy." *Id. See also Engine Mfrs. Ass'n v. S. Coast Air Quality Mgmt.,* 541 U.S. 246, 253-55 (2004) (applying federal statute to preempt state restrictions on vehicle purchasers, although Congress' expressed focus

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[4] The Private Securities Litigation Reform Act of 1995, P.L. 104-67, 109 Stat. 743, 758, *codified at* 15 U.S.C. §§ 77z-1, 78u-4.

was on eliminating the restrictions on manufacturers); *H.J. Inc. v. Northwestern Bell Tel. Co.*, 492 U.S. 229, 245-49 (1989) (recognizing that the language of the RICO statute reaches far more than organized crime and declining to narrow that reach).

Moreover, Congress was well aware that SLUSA precluded a wider range of state law securities suits than those that could have been filed in federal court but were filed in state court to avoid the PSLRA. Some members of Congress, consumer organizations, and law professors had argued strenuously during the legislative process that SLUSA would deprive investors of any remedy at all in many circumstances and should be amended to avoid that. Senators Sarbanes, Bryan and Johnson had filed a separate statement to accompany the committee report from the Senate, stressing that "in too many cases, investors will be left without any effective remedies at all." S. Rep. 105-182, at 11 (1998) (Additional views of Senators Sarbanes, Bryan and Johnson). The statement emphasized that SLUSA would withdraw a number of protections investors had enjoyed under state law, mentioning specifically the ability to impose aiding and abetting liability and longer statutes of limitation. *Id.* at 20-22.

Their argument for amending SLUSA to avoid such broad preemption did not prevail. In addition to closing the PSLRA loophole, the majority was concerned more generally with the harmful effects of subjecting nationally traded securities to state law in private class actions. The PSLRA itself was enacted in reaction to "abuse in private securities lawsuits," which Congress determined was undermining the "integrity of American markets . . . by those who seek to line their own pockets by bringing abusive and meritless suits." H.R. Conf. Rep. No. 104-369 at 31 (1995). But, in the three years following enactment of the PSLRA, Congress' efforts to prevent abusive suits was increasingly thwarted by savvy litigators filing actions against securities companies under state law. 112 Stat. at 3227.

Thus, the Senate Committee noted that "state-court class actions involving nationally traded securities were virtually unknown prior to the [PSLRA, but] they are brought with some frequency now." S. Rep. No. 105-182, at 4 (1998). It expressed concern that "this state class-action trend has . . . created a ripple-effect that has inhibited small, high growth companies in their efforts to raise capital, and has damaged the overall efficiency of our capital markets." *Id.*

After weighing states' rights and federalism interests, it "found the interest in promoting efficient national markets to be the more convincing and compelling consideration in this context," *id.*, because "fraudulent and abusive securities class action litigation distorts the efficient operation of those markets and the optimal allocation of available capital," *id.* at 5. The Conference Committee similarly expressed the concern of majorities in both houses of Congress with plaintiffs' lawyers' "filing frivolous and speculative lawsuits in State court," and "a single state [being able to] impose the risks and costs of its peculiar litigation system on all national issuers." Conf. Rep. at 15.

Whether Congress specifically anticipated every instance in which SLUSA would preempt a state law action that—in fact or as drafted—could not be brought under federal law has no bearing. *See Griffin*, 458 U.S. at 576 (imposing the terms of a statute as written, notwithstanding its conclusion that Congress had not precisely envisioned the result, and noting many other statutes that had been applied as written regardless of whether Congress had anticipated the situation to which they were applied). "[T]he fact that a statute can be applied in situations not expressly anticipated by Congress does not demonstrate ambiguity. It demonstrates breadth." *Pa. Dep't of Corr. v. Yeskey*, 524 U.S. 206, 212 (1998) (quotation omitted).

Thus, whether or not the current rash of securities lawsuits, artfully drafted as state law actions, had been expressly anticipated by Congress, the statute Congress

enacted plainly, and properly, covers them. That Congress' purposes are furthered by SLUSA's preemption of all actions it reaches, regardless of whether the plaintiffs purchased or sold securities, "only underscores [the courts'] duty to refrain from reading a phrase into the statute when Congress has left it out." *Keene*, 508 U.S. at 208.

### D. The Second Circuit's View Is Based on a Misreading of the Statutory Text.

The Second Circuit's conclusion in the instant case—that the purchaser-seller requirement is contained in the "in connection with" language of Section 10(b), and therefore in SLUSA—strayed too far from the statutory text and misread *Blue Chip Stamps*. *See* Pet. App. 52a. The court below offered no explanation as to how the text of Section 10(b) could have one meaning when applied to a case brought by the SEC and another when applied to a case brought by a private plaintiff. The court's conclusion that the SEC could bring a Section 10(b) claim as long as *someone* buys or sells the security during the period of allegedly fraudulent conduct, *id.* at 24a, should have resolved the *statute's* application to all potential plaintiffs. Its reliance upon *Blue Chip Stamps* to supply controlling precedent, in the absence of textual analysis, is misplaced. As discussed above, *Blue Chip Stamps* did not rule that Section 10(b), much less its "in connection with" provision, supplied the purchaser-seller requirement; rather, the Court explained repeatedly that it did not. *See, supra*, Pt. I.

None of the ancillary arguments relied on by the court below apply. Its focus on whether Congress, in enacting SLUSA, had expressly indicated that it intended to reach suits by non-purchasers/non-sellers is backwards. *See* Pet. App. 21a, 27a, 31a. Congress had already indicated it intended to reach such suits by borrowing language that had long been read to reach such suits. The appropriate question would have been whether Congress had expressly indicated that it intended to *exclude* suits by non-purchasers/non-sellers because courts may only disregard statutory

text if there is "something to make plain the intent of Congress that the letter of the statute is not to prevail." *Crooks v. Harrelson*, 282 U.S. 55, 60 (1930). *Accord Tenn. Valley Auth. v. Hill*, 437 U.S. 153, 188 n.33 (1978). There was not. *See, supra*, Pts. II.B&C.

The Second Circuit's reliance on the presumption against preemption is also inapposite. See Pet. App. 30a-31a. Congress provided an *express* preemption provision in SLUSA, leaving "the task of statutory construction . . . in the first instance [to] focus on the plain wording of the clause, which necessarily contains the best evidence of Congress' preemptive intent." *CSX Trans., Inc. v. Easterwood*, 507 U.S. 658, 664 (1993).

Finally, the court below cannot derive support from *Blue Chip Stamps'* conclusion that the purchaser-seller restriction it fashioned would be counterbalanced by the existence of remedies under state law. *See* Pet. App. 29a-30a. *Blue Chip Stamps* noted such remedies in a footnote in its consideration of the practical policies weighing in favor of and against adopting such a limitation on private securities actions. The Court's weighing of the practical implications of a judge-made restriction under consideration has no force in *this* context. Congress has spoken since *Blue Chip Stamps'* policy discussion. It enacted a statute that preempts state law private securities class actions, using language long understood to reach actions by non-purchasers/non-sellers. Therefore, "[t]he issue . . . is not whether [permitting plaintiffs to bring actions under state law that may not be maintained by them under federal law] is good policy but whether [it] is covered by the statute." *Central Bank*, 511 U.S. at 177. Thus, even if the Second Circuit viewed such preemption as unwise or unfair, it may not "substitute its policy judgment for that of Congress." *Hodel v. Indiana*, 452 U.S. 314, 331 (1981).

In sum, SLUSA's "in connection with" requirement, like Section 10(b)'s, is met if the alleged misrepresentations,

omissions or manipulative conduct is connected to *someone's* securities transactions.

## III. APPLICATION OF SLUSA'S "IN CONNECTION WITH" REQUIREMENT TO INDIVIDUAL CASES.

With respect to whether alleged misconduct is connected to someone's securities transactions in a specific case, this Court has repeatedly held, in interpreting Section 10(b), that "in connection with" should be read broadly and flexibiy, not technically and restrictively. *Zandford,* 535 U.S. at 819. In many contexts, such as the market timing class actions, a broad and flexible reading of the "in connection with" requirement is not even needed to find the requirement met. *Amicus* presents its view of SLUSA's application to market-timing class actions in order to inform this Court's framing of its decision, if it reaches the application of SLUSA's "in connection with" requirement to the instant case.

### A. The Market-Timing Class Action Allegations

Many of the market-timing class actions brought over the last two years allege that variable annuity and mutual fund companies facilitated transactions by arbitrageurs that diluted the value of shares owned by longer-term holders, including plaintiffs, by the manner in which they are alleged to have set share prices. Mutual funds, and the subaccounts by which variable annuity contract-holders invest in them, set share prices once a day as of the close of the New York Stock Exchange. These class actions allege that the companies set share prices for these funds and subaccounts based on the most recently available market value for each security. For securities traded in the United States, the most recently available market value is a current price. For securities traded on foreign stock exchanges, the most recently available market value is five to fifteen hours old, because they operate in different time zones.

The class actions allege that arbitrageurs can predict whether foreign securities will rise or fall, based on what has happened in the U.S. markets while the foreign exchanges were closed and other indices, and that the arbitrageurs can therefore time purchases and sales of shares in fund portfolios that include foreign securities to take advantage of the allegedly "stale" pricing. The actions further allege that, by doing so, these market-timers reap profits that would otherwise belong to long-term investors and avoid losses that are left to the long-term investors. They further allege that the companies facilitated the market-timers' transactions and thereby breached duties to their long-term investors by exposing them to dilution of the value of their securities. In some complaints, the class actions allege that the companies failed to disclose that the pricing was "stale," that arbitrage was a risk, and that it would lower the value of securities held long-term.

### B. "In Connection With" Transactions By Market Timers

The first way in which these market-timing class actions meet SLUSA's "in connection with" requirement is by alleging that the variable annuity and mutual fund companies breached their duties by facilitating purchases and sales of covered securities by market timers. The plaintiffs specifically allege both the existence of market-timed securities transactions based on the allegedly wrongful pricing and that these transactions injured them.

Allegations that securities are wrongfully valued concern conduct that is inherently "in connection with" the purchase or sale of securities, because each day's price exists solely to determine how much each investor must pay or will receive for a purchase or sale. Here, in addition, the allegations assert that the defendant's alleged misconduct would not have caused plaintiffs' alleged injuries absent the purchases and sales by the market timers. Thus, the alleged misconduct in market timing class actions is "in connection

with" securities transactions so as to fall within SLUSA's preemptive reach.

### C. "In Connection With" Plaintiffs' Own Purchases, Either Before or During the Class Period.

In addition, as is the case for many state law actions filed on behalf of a class of "holders," the market-timing class actions explicitly or implicitly involve allegations under Section 10(b) and Rule 10b-5, based on plaintiffs' and class members' own securities purchases. In the past two years, hundreds of cases have been brought, complaining of market-timing in mutual funds and variable annuity subaccounts. Most of these have been brought in federal court asserting federal causes of action.

Implicit in any "holder" allegations about market--timing is the complaint that the plaintiffs were misled or manipulated into purchasing the securities. If the plaintiffs had purchased the securities expecting other investors to make market-timed transactions, they would have no basis for complaint. On the other hand, if the securities were represented as arbitrage-proof or if purchasers were assured that market-timed trades would be prevented, Section 10(b) or Rule 10b-5 potentially provides investors claiming to have been harmed by market-timed trades with a means of redress. *See Kircher,* 403 F.3d at 484 ("plaintiffs' claims depend on statements made or omitted in connection with *their own* purchases of the funds' securities").

Indeed, in the original complaint filed against Pacific Life, the plaintiff alleged that the defendant had convinced the plaintiff and other investors to purchase variable annuity contracts by marketing the advantages of long-term ownership of variable annuities over direct investment without providing complete and truthful information to plaintiff and the class about its pricing and the risks of dilution of long-term contract holders' investments as a result of arbitrage facilitated by that pricing. However, in

his current complaint – an effort at SLUSA-proofing the allegations – plaintiff has carefully worded the complaint to focus almost uniformly on conduct that affected him after he purchased the security and has expressly excluded claims based on Pacific Life's conduct in connection with his or class members' purchases or sales of securities.[5] The alleged events out of which these claims arise, and the relief requested, are identical.

If SLUSA is to have the result Congress intended, it is necessary to consider not only the allegations as carefully drafted by counsel eager to avoid SLUSA, but also whether the events complained of necessarily include conduct subject to Section 10(b) and Rule 10b-5 prohibitions, and therefore could have been addressed in a private or government enforcement action under those provisions. Absent the safeguard of considering the underlying nature of the complaint, any but the most inept or inattentive of plaintiffs' counsel will quickly hone the techniques of drafting complaints to avoid preemption. And SLUSA will be rendered wholly ineffective for preventing federal securities fraud actions involving nationally traded securities from being brought in state courts and subjected to varying state laws. Because this "is the very sort of maneuver that SLUSA was designed to prevent," *Kircher*, 403 F.3d at 484, courts must look behind the words of the complaint to determine whether a plaintiff's grievance is properly addressed as a securities fraud claim. *Accord Rowinski v. Salomon Smith Barney Inc.*, 398 F.3d 294, 300 (3d Cir. 2005); *Dudek v. Prudential Sec., Inc.*, 295 F.3d 875, 879-80 (8th Cir. 2002).

With respect to market timing in variable annuity subaccounts and mutual funds, the inherent nature of the claims is rendered particularly apparent by the SEC's

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[5] Plaintiff voluntarily dismissed his first complaint and filed a redrafted complaint soon thereafter.

decisions to bring such claims under Section 10(b) and Rule 10b-5, and to successfully settle them.[6]

Such actions meet the "in connection with" requirement of Section 10(b) and Rule 10b-5 because the defendants' alleged misconduct is "in connection with" the purchases of investors who were misled. That connection provides a second basis for finding that private class actions arising out of market-timed trades meet SLUSA's "in connection with" requirement.

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[6] *See, e.g., In re CIHC, Inc.*, No. 3-11578, Securities Act Release No. 8455, Exchange Act Release No. 50165, Investment Co. Act Release No. 26526 (Aug. 9, 2004) (SEC found, in connection with settlement, that defendants, including issuer of variable annuity products, violated Section 10(b) and Rule 10b-5 by misrepresenting that action would be taken to limit market timing and then facilitating market-timed transactions); *In re Inviva, Inc.*, No. 3-11579, Securities Act Release No. 8456, Exchange Act Release No. 50166, Investment Co. Act Release No. 26527 (Aug. 9, 2004) (same).

## CONCLUSION

For the foregoing reasons, the Court should rule that the *Blue Chip Stamps* purchaser-seller limitation was not incorporated into SLUSA, and does not confine SLUSA's preemptive scope. Thus, many "holder" allegations allege misconduct "in connection with" securities transactions and therefore within SLUSA's preemptive reach.

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IN THE

# Supreme Court of the United States

MERRILL LYNCH, PIERCE, FENNER & SMITH, INC.,
*Petitioner,*

v.

SHADI DABIT, on behalf of himself and all others similarly situated,
*Respondents.*

**On Writ of Certiorari to the United States Court of Appeals for the Second Circuit**

## BRIEF *AMICI CURIAE* OF THE SECURITIES INDUSTRY ASSOCIATION AND THE BOND MARKET ASSOCIATION IN SUPPORT OF PETITIONER

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## QUESTION PRESENTED

Whether the preemption provision of the Securities Litigation Uniform Standards Act, which bars class actions based upon state law that allege "a misrepresentation or omission of a material fact in connection with the purchase or sale of a covered security," applies to securities class actions by persons who allege they held securities in reliance upon a misrepresentation or omission about a covered security.

TABLE OF CONTENTS


| | Page |
|---|---|
| QUESTION PRESENTED | i |
| TABLE OF AUTHORITIES | v |
| INTEREST OF THE *AMICI CURIAE* | 1 |
| STATUTORY PROVISIONS INVOLVED | 3 |
| INTRODUCTION AND SUMMARY OF ARGUMENT | 4 |
| ARGUMENT | 7 |
| I. THE NATURAL MEANING AND POLICY OF THE SLUSA PREEMPTION PROVISION REQUIRES PREEMPTION OF HOLDER CLASS ACTIONS | 7 |
| A. The Text Of SLUSA Supports Preemption | 7 |
| B. This Court's Interpretation Of Section 10(b) In *O'Hagan* Cannot Be Squared With A Non-Preemptive Reading Of SLUSA | 10 |
| C. *Blue Chip Stamps* Was Not Based On An Interpretation Of The "In Connection With" Language | 11 |
| D. SLUSA's Policy Of Achieving Uniformity In The Standards Governing U.S. Securities Litigation Supports Preemption | 13 |
| II. NO POLICY RATIONALE SUPPORTS READING SLUSA NOT TO PREEMPT HOLDER CLASS ACTION STATE LAW CLAIMS | 15 |
| A. The Non-Preemptive Reading Of SLUSA Would Illogically Create Greater Potential Remedies For Holders Of Securities Than For Purchasers And Sellers | 15 |

TABLE OF CONTENTS – continued

Page

B. A Class Of Holders Of Securities Cannot Be Injured By A Misrepresentation ..... 17

III. SLUSA'S LEGISLATIVE HISTORY DOES NOT SUPPORT AN EXCEPTION FOR HOLDER CLASS ACTION STATE LAW CLAIMS ..... 19

CONCLUSION ..... 21

## TABLE OF AUTHORITIES

CASES Page

*Arent* v. *Distribution Scis., Inc.*, 975 F.2d 1370 (8th Cir. 1992) ..... 18
*Basic, Inc.* v. *Levinson*, 485 U.S. 224 (1988) ..... 9, 18
*Blue Chip Stamps* v. *Manor Drug Stores*, 421 U.S. 723 (1975) ..... 5, 12, 13, 14
*Burns* v. *Prudential Secs.*, 116 F. Supp. 2d 917 (N.D. Ohio 2000) ..... 20
*Chanoff* v. *United States Surgical Corp.*, 857 F. Supp. 1011 (D. Conn.), *aff'd*, 31 F.3d 66 (2d Cir. 1994) ..... 18
*Crocker* v. *FDIC*, 826 F.2d 347 (5th Cir. 1987) ... 17, 18
*Dura Pharms., Inc.* v. *Broudo*, 125 S. Ct. 1627 (2005) ..... 2, 8, 9, 14, 18
*Edgar* v. *MITE Corp.*, 457 U.S. 624 (1982) ..... 21
*Ernst & Ernst* v. *Hochfelder*, 425 U.S. 185 (1976) ..... 16
*Ganino* v. *Citizens Utils. Co.*, 228 F.3d 154 (2d Cir. 2000) ..... 16
*Green* v. *Ameritrade, Inc.*, 120 F. Supp. 2d 795 (D. Neb. 2000), *aff'd on other grounds*, 279 F.3d 590 (8th Cir. 2002) ..... 20
*Holmes* v. *Securities Investor Prot. Corp.*, 503 U.S. 258 (1992) ..... 10, 12
*Howsam* v. *Dean Witter Reynolds, Inc.*, 537 U.S. 79 (2002) ..... 2
*Kagan* v. *Edison Bros. Stores, Inc.*, 907 F.2d 690 (7th Cir. 1990) ..... 18
*Kircher* v. *Putnam Funds Trust*, 403 F.3d 478 (7th Cir. 2005), *rehearing denied*, 2005 U.S. App. LEXIS 7914 (7th Cir. May 2, 2005), *petition for cert. filed*, No. 05-409 (U.S. Sept. 29, 2005) ..... 5, 20
*Lampf, Pleva, Lipkind, Prupis & Petigrow* v. *Gilbertson*, 501 U.S. 350 (1991) ..... 2

TABLE OF AUTHORITIES – continued

Page

*Levine* v. *Seilon, Inc.*, 439 F.2d 328 (2d Cir. 1971) ..... 7, 18
*Metropolitan Life Ins. Co.* v. *Massachusetts*, 471 U.S. 724 (1985) ..... 13
*Morales* v. *Trans World Airlines, Inc.*, 504 U.S. 374 (1992) ..... 7, 20
*Pelletier* v. *Stuart-James Co.*, 863 F.2d 1550 (11th Cir. 1989) ..... 16
*Rieger* v. *Drabinsky (In re Livent, Inc. Noteholders Sec. Litig.)*, 151 F. Supp. 2d 371 (S.D.N.Y. 2001) ..... 15
*Rodriguez De Quijas* v. *Shearson/Am. Express, Inc.*, 490 U.S. 477 (1989) ..... 2
*Scheidler* v. *National Org. for Women, Inc.*, 537 U.S. 393 (2003) ..... 10
*Shearson/Am. Express, Inc.* v. *McMahon*, 482 U.S. 220 (1987) ..... 2
*State Farm Mut. Auto. Ins. Co.* v. *Campbell*, 538 U.S. 408 (2003) ..... 21
*United States* v. *O'Hagan*, 521 U.S. 642 (1997) ..... 5, 6, 10, 11, 12
*Voskamp* v. *Arnoldy*, 749 S.W.2d 113 (Tex. App. 1987) ..... 16

STATUTES

15 U.S.C. § 77k(a) ..... 9
§ 77l(a) ..... 9
§ 77r(b) ..... 8
§ 78j(b) ..... 4
§ 78r(a) ..... 9
§ 78t-1(a) ..... 9
§ 78u-4(b)(3) ..... 16
§ 78bb ..... *passim*

TABLE OF AUTHORITIES – continued


| | Page |
|---|---|
| 28 U.S.C. § 1453(d)(1) | 14 |
| § 1658(b) | 16 |
| Ind. Code Ann. § 23-2-1-19(g) | 16 |
| N.H. Rev. Stat. Ann. § 421-B:25(VII) | 16 |
| S.C. Code Ann. § 35-1-1530 | 16 |
| Wash. Rev. Code § 21.20.430(4)(b) | 16 |
| **RULE** | |
| Fed. R. Civ. P. 9(b) | 16 |
| **LEGISLATIVE HISTORY** | |
| S. Rep. No. 105-182 (1998) | 13 |
| S. Rep. No. 109-14 (2005) | 14 |
| 143 Cong. Rec. S10475 (daily ed. Oct. 7, 1997), *available at* 1997 WL 614735 | 14, 15, 19 |
| **OTHER AUTHORITIES** | |
| Securities Industry Association, *at* http://www.sia.com (last visited Nov. 14, 2005) | 1 |
| The Bond Market Association, *at* http://www.bondmarkets.com (last visited Nov. 14, 2005) | 2 |

## INTEREST OF THE *AMICI CURIAE*[1]

The Securities Industry Association ("SIA") brings together the shared interests of approximately 600 securities firms to accomplish common goals. SIA's primary mission is to build and maintain public trust and confidence in the securities markets. SIA members (including investment banks, broker-dealers, and mutual fund companies) are active in all U.S. and foreign markets and in all phases of corporate and public finance. According to the Bureau of Labor Statistics, the U.S. securities industry employs nearly 800,000 individuals, and its personnel manage the accounts of nearly 93 million investors directly and indirectly through corporate, thrift, and pension plans. In 2004, the industry generated $236.7 billion in domestic revenue and an estimated $340 billion in global revenues. (More information about SIA is available at www.sia.com.)

The Bond Market Association ("TBMA") represents approximately 200 securities firms and banks that underwrite, trade and sell fixed-income securities in the United States and in international markets. TBMA's members transact business in a wide variety of public and private fixed-income securities. Its membership comprises a diverse mix of securities firms and banks, including large, multi-product firms and companies with special market niches. It includes all primary dealers in U.S. government securities, as recognized by the Federal Reserve Bank of New York, and all major dealers in federal agency securities, mortgage-backed and asset-backed securities, corporate bonds, money market instruments, and funding instruments such as repurchase and

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[1] Pursuant to this Court's Rule 37.6, *amici* SIA and TBMA state that no counsel for any party authored this brief in whole or in part, and no person or entity other than *amici* and their members made a monetary contribution to the preparation or submission of the brief. Counsel of record for both parties have consented to the filing of this brief, and the letters of consent have been filed with the Clerk.

securities lending agreements. From its inception in 1976, TBMA has worked with its member firms, Congress, the SEC, the Federal Reserve Board and the Federal Reserve Bank of New York, state regulators, and self-regulatory organizations to foster effective, efficient regulation; to enhance the liquidity and efficiency of the fixed income markets; to encourage sound credit and business practices for participants in such markets; and to promote the highest levels of professional standards and conduct in such markets. TBMA's efforts to encourage efficient regulation of U.S. markets serves to encourage foreign as well as domestic securities issuance in the United States. In 2004, there were $46.4 billion in dollar-denominated debt securities issued in the United States by foreign companies, most through TBMA members.[2] (More information about TBMA is available at www. bondmarkets.com.)

The SIA and/or TBMA have previously filed *amici* briefs with the Court in cases affecting civil liability and the federal securities laws. See, *e.g.*, *Dura Pharms., Inc.* v. *Broudo*, 125 S. Ct. 1627 (2005); *Howsam* v. *Dean Witter Reynolds, Inc.*, 537 U.S. 79 (2002); *Lampf, Pleva, Lipkind, Prupis & Petigrow* v. *Gilbertson*, 501 U.S. 350 (1991); *Rodriguez De Quijas* v. *Shearson/Amer. Express, Inc.*, 490 U.S. 477 (1989); *Shearson/Amer. Express, Inc.* v. *McMahon*, 482 U.S. 220 (1987).

The issue raised by this case is whether holders of securities who refrained from selling, i.e., those who held onto securities, in reliance upon an alleged misrepresentation can bring state-law class actions that survive the preemption provision of the Securities Litigation Uniform Standards Act ("SLUSA"). This issue is one of great import to the securities industry and investors in this era of proliferating securities litigation. It is critically important to the SIA and TBMA that

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[2] This figure does not include foreign issues with maturities of one year or less, certificates of deposit, or convertible bonds.

the effort of Congress to curb vexatious litigation in state law securities class actions by enacting the uniform national requirements of SLUSA, not fall prey to plaintiffs who attempt creatively to plead around SLUSA preemption and the stricter federal securities standards. Such uniform standards are critical to the use of U.S. securities markets by both domestic and foreign issuers. *Amici* therefore have a vital interest in the issue presented in this case, and their views and experience can assist the Court in resolving that issue.

## STATUTORY PROVISIONS INVOLVED

Securities Litigation Uniform Standards Act:

> No covered class action based upon the statutory or common law of any State or subdivision thereof may be maintained in any State or Federal court by any private party alleging – (A) a misrepresentation or omission of a material fact in connection with the purchase or sale of a covered security; or (B) that the defendant used or employed any manipulative or deceptive device or contrivance in connection with the purchase or sale of a covered security.

15 U.S.C. § 78bb(f)(1).

Securities and Exchange Act § 10(b):

> It shall be unlawful for any person, directly or indirectly, by use of any means or instrumentality of interstate commerce or of the mails, or of any facility of any national securities exchange . . . (b) To use or employ, in connection with the purchase or sale of any security registered on a national securities exchange or any security not so registered, or any securities-based swap agreement . . . any manipulative or deceptive device or contrivance in contravention of such rules and regulations as the Commission may prescribe as

necessary or appropriate in the public interest or for the protection of investors.

15 U.S.C. § 78j(b).

## INTRODUCTION AND SUMMARY OF ARGUMENT

This case presents the question whether the SLUSA preemption provision applies to state law class action claims brought by holders of securities. An illustration will demonstrate the vastly different outcomes under the conflicting approaches. Suppose H buys stock at a price of $40 per share in defendant D *before* any alleged fraud. As time passes, the stock price climbs to $50. D allegedly suffers a business setback that it conceals for a period of time. *After* the alleged concealment begins, P purchases D's stock at $50 per share. Later, when the setback is subsequently disclosed, D's stock price drops to $30. H has remained a holder of D's stock throughout.

P brings a federal § 10(b) class action alleging that the concealment caused those who purchased after the concealment began to suffer a loss from the post-purchase decline caused by the disclosure of the setbacks. Of course, the purchaser class action may proceed.

Separately, H brings a class action based on state law alleging that the concealment caused the holder class to refrain from selling at the $50 price.[3] This case concerns whether the holder class action may proceed in state court. The position of respondents and the plaintiff class action bar is that the holder case proceeds. Under their approach, the holder's state law class action would probably sue for both fraud and negligence, and for both compensatory and punitive damages, "in the hope that a local judge or jury may produce

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[3] As we demonstrate *infra* at 17-18, the premise that a class of holders could have sold at the $50 price if the truth were disclosed earlier is economic nonsense.